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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1942

No. 1000

THE PETTICREW REAL ESTATE COMPANY,
BANKRUPT,
Petitioner,

vs.

HARRY MUFFLER, AS RECEIVER OF THE PETTICREW REAL ESTATE COMPANY, THE MERCHANTS AND MECHANICS FEDERAL SAVINGS & LOAN ASSOCIATION, AND THE SPRINGFIELD FEDERAL SAVINGS & LOAN ASSOCIATION.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

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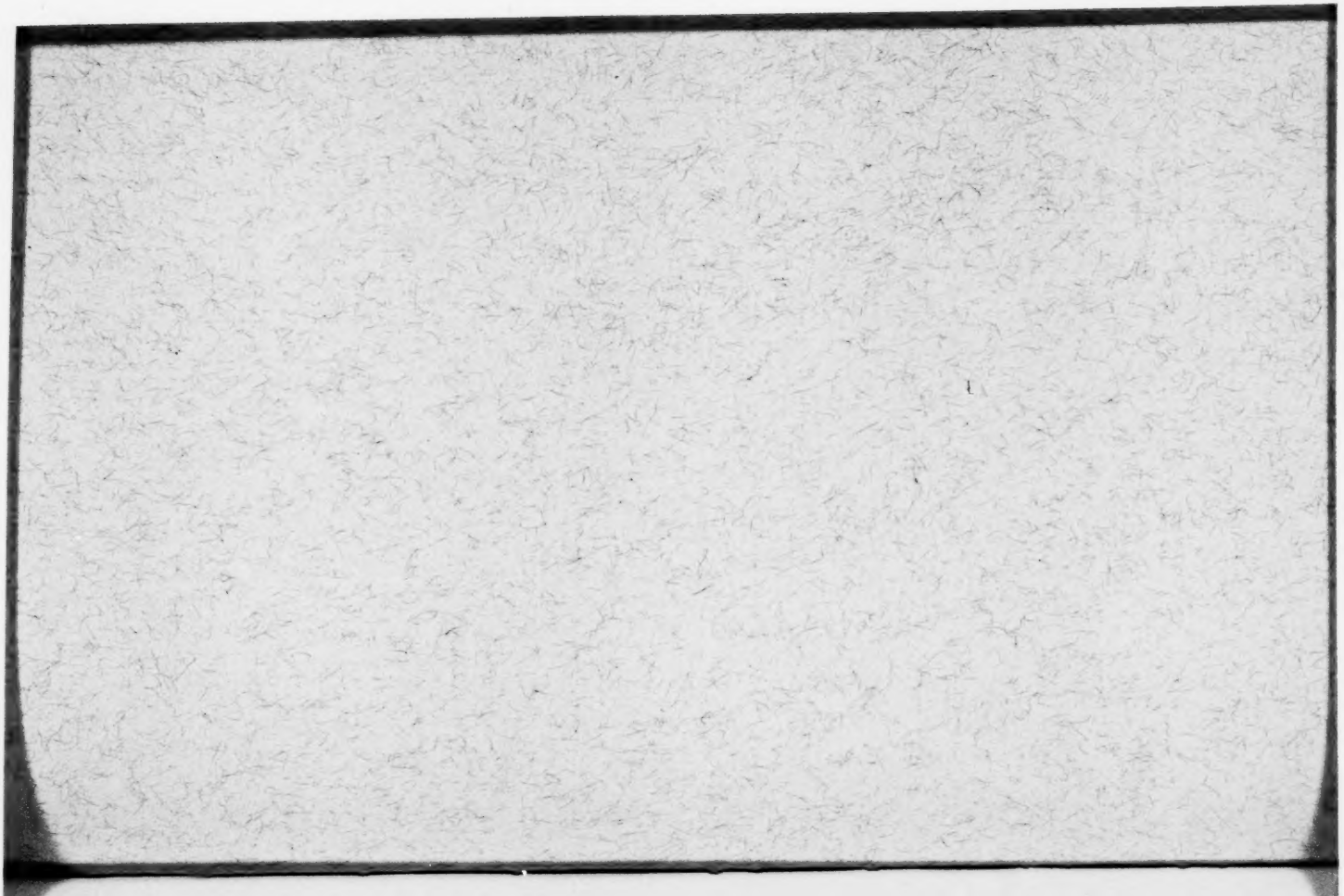

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To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

Summary Statement of Matters Involved.

This case challenges the jurisdiction of the United States District Court in a bankruptcy proceeding where, upon the filing of a petition in bankruptcy, the United States District Court for the Southern District of Ohio, Western Division, issued an order restraining and staying all acts and pro-

ceedings to enforce any lien upon the property of the bankrupt, and he continuation of any suit or proceeding against it until further order of the court.

Harry Muffler, as Receiver of The Petticrew Real Estate Company, the Merchants and Mechanics Federal Savings & Loan Association, and the Springfield Federal Savings & Loan Association, moved for an order dissolving the restraining order, vacating the adjudication of bankruptcy and the order of reference, and dismissing the petition. This motion was denied by the District Court. Whereupon an appeal was prosecuted to the United States Circuit Court of Appeals of the Sixth Circuit from the denial of this motion. Said United States Circuit Court of Appeals in an opinion filed December 1, 1942, affirmed that part of the order denying the motion to vacate the adjudication of bankruptcy and the order of reference, and to dismiss the petition, but that part of the order which denied the motion to vacate the restraining order was reversed, and the case was remanded to the District Court for further proceedings in accordance with that opinion. A motion for rehearing was filed by The Petticrew Real Estate Company, and said United States Circuit Court of Appeals on February 4, 1943, modified its opinion, the modification being as follows. In the original opinion said Circuit Court of Appeals said:

> "* * * However, we think another feature of the case decisive. Since the liens matured more than four months before the present bankruptcy proceedings, and the action to enforce the liens in the state court antedated the filing of the bankruptcy petition, and since the state court had possession of the property, it has exclusive jurisdiction thereof and the District Court, under the decisions of the Supreme Court, was required to dissolve the stay."

After the application for rehearing was filed, said Circuit Court of Appeals on February 4, 1943, struck out the

word "thereof" in the above paragraph, and substituted the following words: "To foreclose the mortgages thereon."

The undisputed facts pertinent to this motion are as follows:

(1) Prior to March 5, 1933, Petitioner was a corporation doing a general real estate business in the city of Springfield, Ohio. The Merchants and Mechanics Federal Savings & Loan Association, and the Springfield Federal Savings & Loan Association, held mortgages upon many parcels of real property then owned by Petitioner.

On March 5, 1933, a receivership proceeding was instituted in the State court and on March 8, 1933, a receiver was appointed, to-wit, Harry Muffler, who took possession of the assets of the corporation, including the real estate.

On February 16, 1938, the receiver filed a petition in the State court, praying that liens be marshaled, that the mortgaged real estate be sold, and for other equitable relief. No deficiency judgment was asked.

The case proceeded in the State Court upon said petition to sell said real estate filed by the receiver on February 16, 1938. The case lay dormant for several years.

(2) On March 16, 1942, the State court entered an order, part of which is as follows:

> "The Court further finds from the evidence that the defendant herein, The Petticrew Real Estate Company, is insolvent and that its assets at their fair, reasonable market value are grossly inadequate to pay, satisfy and discharge the just debts and obligations of said company and that said condition has existed continuously, and did so exist at and prior to the appointment of the receiver herein. The Court further finds that the real estate herein ordered sold as aforesaid constitutes practically all of the assets of said corporation, that said corporation was engaged prior to the receiver-

ship in buying, selling and the development of real estate and that in the event the real estate herein ordered sold has not been redeemed as herein provided, and is sold as herein ordered and decreed, that it is equitable and proper that the receiver herein proceed to wind up the affairs of said corporation and dissolve the same and to sell and distribute the remaining assets of said corporation and apply the proceeds thereof as directed by the Court and that said receiver shall hereafter in such event proceed to make the proper and necessary application or applications and institute the necessary and proper action or actions and proceedings to carry into effect this order and decree.

(3) On April 16th, 1942, and before any appraisement or advertising of sale had been had under the order of sale by the Sheriff of Clark County, The Petticrew Real Estate Company filed its voluntary petition in bankruptcy in the District Court in this cause, upon which an order of adjudication of bankruptcy and reference was entered by the Court on the same day. On the same date, the bankrupt filed its petition in this cause for a stay of the proceedings in the Court of Common Pleas of Clark County, Ohio, upon which, on the same day, April 16th, 1942, the restraining order hereinabove referred to was issued by the United States District Court.

Reasons Relied Upon for the Allowance of the Writ.

By its decision and mandate said United States Circuit Court of Appeals held that when a State court receiver takes possession and custody of real estate, on which real estate there are liens which matured more than four months before the bankruptcy proceedings, it had exclusive jurisdiction to foreclose the mortgages thereon, even though the petition of the receiver to sell the real estate was filed on February 16, 1938, and no court order granting the receiver the right to sell the real estate was made until March 16,

1942, which was thirty days before the petition in bankruptcy was filed. Said United States Circuit Court of Appeals relied in making its decision on the case of *Straton* v. *New*, 283 U. S. 318 (and similar decisions). In the decision of said United States Circuit Court of Appeals it said:

> "Under Ohio law a mortgage upon real estate is a lien from time of record (General Code of Ohio, Section 8542; *Stewart* v. *Hopkins*, 30 Ohio St. 502; *In re Farm and Home Co.*, 84 Fed. (2d) 933, 935 (C. C. A. 6).) The validity of the mortgages is not questioned and they had matured through record a number of years prior to the filing of the bankruptcy petition. The petition for their enforcement had been filed in the state court more than four years before the instant bankruptcy petition was filed. The case therefore seems to be squarely governed by *Straton* v. *New*, 283 U. S. 218; *Dannel* v. *Wilson-Weesner-Wilkinson Co.*, 109 Fed. (2d) 364 (C. C. A. 6), and similar decisions, and to require the conclusion that the District Court erred in denying the motion to vacate the restraining order. *Straton* v. *New* declared that liens acquired more than four months before the bankruptcy proceedings are instituted, if valid under state law, are preserved and will be accorded priority by the bankruptcy court in distribution of the estate in accordance with applicable local law. It also declared that when under liens thus acquired prior to the four months' period the state court has taken possession of the res for the purpose of enforcing the lien, the District Court sitting in bankruptcy has no power to enjoin the continuation of such action. See *Beeler* v. *Schumacher*, 80 Fed. (2d) 715 (C. C. A. 6). Cf. *In re Conservative Mortgage & Guaranty Co.*, 24 Fed. (2d) 38 (C. C. A. 6), and *Willis* v. *Beeler*, 90 Fed. (2d) 538, 542 (C. C. A. 6.)

Straton v. *New*, supra, lays down twelve principles of law, as follows:

> (1) The purpose of the Bankruptcy is to place the property of the bankrupt, wherever found, under the

control of the court for equal distribution among creditors.

(This is our contention.)

(2) Jurisdiction of a bankruptcy court over the estate of the bankrupt is exclusive within the field defined by the Bankruptcy Act.

(This is our contention.)

(3) Jurisdiction of a bankruptcy court over the property of the bankrupt is so far in rem that the estate is regarded as in custodia legis from the filing of the petition.

(This is our contention.)

(4) After the filing of a petition in bankruptcy, liens cannot be thereafter obtained, nor proceedings had in other courts, to reach the property of the bankrupt, the district court having acquired the exclusive right to administer all property in the bankrupt's possession.

(This is our contention.)

(5) A Federal district court, having acquired by the filing of a petition in bankruptcy the exclusive right to administer the bankrupt's property, may inquire into the validity of liens, marshal them, and control their enforcement and liquidation.

(This is our contention.)

(6) Though a lien be not discharged by bankruptcy, its owner may not without permission of the bankruptcy court, institute proceedings in a state court to enforce it.

(Not applicable.)

(7) A mortgagee may be restrained from instituting or proceeding further in a foreclosure action against a bankrupt, begun after the date of the petition in bankruptcy. (Not applicable.)

(8) A creditor holding a valid judgment against a bankrupt more than four months prior to the date of filing the petition in bankruptcy will be enjoined from

enforcing his lien by suit brought after the date of the petition. (Not applicable.)

(9) As the lien of a judgment entered within four months is avoided in bankruptcy, the court of bankruptcy has jurisdiction to administer the property regardless of the lien, and will restrain the prosecution of an action to enforce it. (Not applicable.)

(10) Liens acquired by legal proceedings more than four months before the filing of a petition in bankruptcy will, if valid under state law, be accorded priority by the bankruptcy court in distribution of the estate, in accordance with applicable local law. (This is our contention.)

(11) Where creditors have obtained and docketed judgments constituting liens on the real estate of the judgment debtor, and have instituted a creditors' suit in a state court to marshal and enforce the liens and sell the real estate subject thereto, the bankruptcy of the judgment debtor occurring four months after the institution of the creditors' suit does not oust the state court of jurisdiction, or vest in the bankruptcy court power to enjoin further proceedings in the state court, *such a proceeding not being in the nature of a proceeding to distribute assets among creditors,* and discharge the debtor from further liability, but merely a proceeding in equity to do what would be done by a sheriff or marshal under an appropriate writ for the sale of real estate in execution at law. (Italics ours.) (Discussed below.)

(12) The Supreme Court takes judicial notice of state statutes.

Obviously, the eleventh of the above principles enunciated by the Supreme Court is the one upon which said United States Circuit Court of Appeals based its opinion. Yet the distinction between it and the case at bar is most evident. By some almost unbelievable coincidence, the verbiage used by the state court in its entry above quoted

is almost identically the positive of what the Supreme Court said must be negative.

The state court said in its entry (Page 79, R.) "that the receiver herein proceed to wind up the affairs of said corporation and dissolve the same and sell and *distribute the remaining assets of said corporation* * * *".

The Straton case says the state court is not ousted of jurisdiction if "such a proceeding is *not* in the nature of a proceeding to distribute assets * * *".

In other words, the instant case, from the state court's own words, is the direct antithesis of the Straton case.

Petitioner contends that by its decision the said United States Circuit Court of Appeals has practically overruled the Supreme Court of the United States on this question.

The said Circuit Court of Appeals has also by its decision reversed other federal authorities, to-wit: *New River Coal Land Co.* v. *Ruffner Brothers,* 165 Fed. Reporter 881, which held, "A District Court, as a Court of Bankruptcy, has exclusive power to determine whether a unit pending in the state court should be stayed or not, and the exercise of this power rests in the discretion of the Judge, which will not be reviewed by an Appellate Court unless it appears to have been abused." (Also forty-seven other cases which followed said *New River Coal Land Co.* v. *Ruffner Brothers.*)

Said Circuit Court of Appeals for the Sixth Circuit did *not* find that the discretion of the United States District Court, which had exclusive jurisdiction, was abused. The question of abuse of discretion was never pressed by opponents.

In *Mortgage Loan Co. et al.* v. *Livingston,* 78 F. (2d) 520, it was held that

> "The position of appellants is that, before a foreclosure suit can be stayed on bankruptcy of the mort-

gagor its trustee must show that there is an equity in the mortgaged property for the bankrupt estate * * *

"The effect of the action of the District Court in denying foreclosure cannot be so narrowly and strictly defined. The determination of whether a mortgagee shall be permitted to foreclose rests in the sound discretion of the Bankruptcy Court. *Title & Trust Co.* v. *Wernich,* 68 F. (2d), 811, 814.

"While valid liens existing at the commencement of a bankruptcy proceedings are preserved, it is solely within the power of a Court of Bankruptcy to ascertain their validity and amount and to decree the method of their liquidation."

By the decision of said United States Circuit Court of Appeals, the sanctity of Federal jurisdiction over bankruptcy proceedings has been theoretically and nominally upheld. However, in all of its practical aspects, it has stripped the bankruptcy court of all right of discretion, as the decisions almost unanimously support. For all practical purposes, this Court has given the state court exclusive jurisdiction.

Said United States Circuit Court of Appeals said in its opinion:

"* * * the liens are valid from time of record and we must accept the finding of the state court made in the proceeding, which opinion antedated the filing of the bankruptcy petition, that the mortgagees were entitled to foreclose in 1933."

We submit that there is no question as to the validity of the liens from the time of record being the law of Ohio, but something more than the liens being valid must occur in order to give jurisdiction to a state court when a federal court intervenes. It is true that the proceedings antedated the filing of the bankruptcy petition and that the mortgagees

were entitled to foreclose in 1933, but we earnestly submit that that, ipso facto, does not give the state court jurisdiction ahead of the federal court.

These mortgages were merely matters of record for all of these years, and the petition that the court speaks about was permitted to lay dormant from 1938 on. In other words, the mortgages, while alive legally, were dead as far as any action was concerned, and when they were finally revitalized and came to life again, they did so thirty days prior to the time that the petition in bankruptcy was filed. Hence the fact that the liens were valid and the fact that the mortgagees could have foreclosed them in 1933 means nothing, in our humble opinion, as far as the jurisdiction of the United States Court is concerned. It was when the mortgagees decided to act on these liens and took a judgment that the bankrupt came into the United States District Court, and the bankrupt came in seasonably.

The distinction between the eleventh syllabus and the case at bar is most evident. In *Stratton* v. *New*, supra, the Supreme Court said that such a proceeding not being in the nature of a proceeding to distribute assets among creditors, but merely being a proceeding in equity, did not oust the state court of jurisdiction. However, in the case at bar the order of the state court as shown at page 79 of the record is that:

> "* * * the receiver herein proceed to wind up the affairs of said corporation and dissolve the same and sell and distribute the remaining assets of said corporation * * *"

Consequently, we contend that said United States Circuit Court of Appeals recognized in its opinion the right of the state court to liquidate the corporation, which this court, we respectfully submit, had no right to do.

In addition to the above relative to *Stratton* v. *New*, syllabus eleven, the Supreme Court specifically states:

> "Where creditors have obtained and docketed judgments constituting liens on the real estate of the judgment debtor and have instituted a creditors' suit in a state court to marshal and enforce the liens and sell the real estate subject thereto, the bankruptcy of the judgment debtor occurring four months after the institution of the creditors' suit does not oust the state court of jurisdiction * * *"

How different such a situation is from the instant case. There was no judgment obtained or docketed in the instant case until less than thirty days prior to the time that the bankruptcy proceeding was filed. In other words, the Building and Loan Associations hereinabove referred to, had no judgment lien on the real estate belonging to the bankrupt that had been obtained and docketed until within thirty days of the date of the filing of the petition in bankruptcy.

We feel, therefore, that for all practical purposes the decision of the United States Circuit Court of Appeals in the instant case definitely reverses all of the prior determinations of this matter by the Supreme Court of the United States.

When these judgments and orders of foreclosure were made by the State Court, then for the first time these liens became judgment liens. Therefore they became judgment liens within four months of the filing of the bankruptcy petition, and nobody but the United States District Court and the higher United States courts have the right to determine whether or not they are valid liens. That is the purpose of the provision concerning judgment liens in the Bankruptcy Act.

Therefore Petitioner feels that because of the conflicts in opinions hereinabove referred to, that the Honorable Su-

preme Court of the United States should hear and determine this matter.

WHEREFORE your Petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court directed to the United States Circuit Court of Appeals for the Sixth Circuit, commanding that court to certify and to send to this Court for its review and determination, on a day certain to be therein named, a transcript of the record and proceedings herein; and that the decree of the United States Circuit Court of Appeals for the Sixth Circuit be reversed by this Honorable Court, and your Petitioner have such other and further relief in the premises as to this Honorable Court may seem meet and just.

SIDNEY G. KUSWORM,
Counsel for Petitioner.

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